

ARTHUR CHAPMAN

KETTERING SMETAK & PIKALA, P.A.

ATTORNEYS AT LAW

2016 MINNESOTA CONSTRUCTION LAW SEMINAR
OCTOBER 13, 2016 | MINNEAPOLIS HILTON | MINNEAPOLIS, MINNESOTA

AGENDA

- 12:30 – 1:00 p.m. **Registration**
- 1:00 – 1:15 p.m. **Welcome**
- 1:15 – 1:45 p.m. **Navigating the Waters of Performance and Payment Bonds** ~ *Stephen M. Warner and Paul S. Almen*
Steve and Paul will examine what contractual clauses are contained in typical performance and payment bonds, and how those clauses impact you. They will also discuss requirements to perfect claims on performance and payment bonds, and the impact on parties to the bonds.
- 1:45 – 2:15 p.m. **Surprised by Employment - Misclassification Issues in Minnesota's Construction Industry** ~ *Kafi C. Linville and Jeffrey M. Markowitz*
Misclassification litigation is on the rise, in fields including the construction industry. Kafi and Jeff will discuss what you can do to avoid misclassification issues under Minnesota construction law, and what you can do if a lawsuit lands on your desk in which a construction worker claims to be an employee misclassified as an independent contractor.
- 2:15 – 2:45 p.m. **Risk or Reward?** ~ *Mark Chauvin of Wiss, Janney, Elstner Associates, Inc.*
Many condominium associations have elected to commence repairs during on-going construction defect litigation. Mark will utilize a few case studies to review and discuss this trend and highlight potential complications.
- 2:45 – 3:00 p.m. **Refreshment Break**
- 3:00 – 3:30 p.m. **Multi-State Construction** ~ *Jonathon M. Zentner and Gregory J. Duncan*
Minnesota, Wisconsin, and North Dakota: Construction defect claims in each of these states have similarities and differences. Hear from our lawyers licensed in each of these states on how state specific laws impact claims handling.
- 3:30 – 4:00 p.m. **Coverage/Legislative Update** ~ *Steven J. Erffmeyer and Corey S. Bronczyk*
Steve and Corey will discuss recent legislative actions of interest to the construction industry and current trends following the 2013 amendments to Minn. Stat. §337.05. They will also discuss insurance coverage for insured contracts under CGL policies.
- 4:00 – 4:30 p.m. **Drones in Construction: Technology, Laws and Insurance** ~ *Mike Korman of Right Stuff Drones*
Mike will cover construction uses for drones; FAA regulations for drone use in commercial operations; questions to ask your drone operator; developing a drone and aviation compliance program for your business; and State of MN Commercial Drone Operator requirements.
- 4:30 – 4:45 p.m. **Question & Answer Session**
- 4:45 – 6:00 p.m. **Reception**

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PERSONNEL QUALIFICATIONS

Mark R. Chauvin | Associate Principal and Unit Manager



EXPERIENCE

Mark Chauvin joined WJE in 1999 and has significant experience with forensic investigations of a wide variety of architectural and structural problems with buildings, facades and bridges. His work has involved inspection, analysis and repair of structural capacity issues, deterioration, distress, or failure of wood, concrete, masonry, steel and post-tensioning systems, including multiple collapse investigations. Mr. Chauvin has also performed numerous investigations of performance problems related to EIFS and stucco claddings, brick masonry facades, and roofing and waterproofing systems.

In addition to his project work, Mr. Chauvin has conducted research to assess the effectiveness of several corrosion mitigation and rehabilitation alternatives on a chloride-contaminated reinforced concrete bridge in Minneapolis.

REPRESENTATIVE PROJECTS

Bridge Engineering

- Lowry Avenue Bridge - Minneapolis, MN: Instrumentation and monitoring of pier movement
- Martin Olav Sabo Pedestrian Bridge - Minneapolis, MN: Evaluation and repair of stay-cable failures
- Minnesota Bridge 02037W - Coon Rapids, MN: Inspection, repair and corrosion monitoring of post-tensioned tendons
- Post-Tensioned Box Girder Bridges - Minnesota: Inspection and assessment of tendon- grouting conditions and materials

Facade Assessment

- Federal Reserve Bank of Minneapolis - Minneapolis, MN: Investigation and repair of leakage and condensation issues
- Kilowatt Community Center - Granite Falls, MN: Investigation and repair of building envelope leakage
- Lincoln Borglum Visitor Center, Mount Rushmore - Keystone, SD: Inspection of granite facade distress
- The Falls at Riverplace - Minneapolis, MN: Investigation of building envelope leakage
- The Metropolitan Opera House - New York, NY: Inspection of travertine facade distress

Failure Investigation

- I-35W Bridge - Minneapolis, MN: Investigation of collapse
- Heritage Lutheran Church - Apple Valley, MN: Investigation of roof collapse
- Life Time Fitness - Savage, MN: Evaluation of precast-plank collapse
- Manufacturing Facility - Cedar Rapids, IA: Investigation of partial roof collapse
- Manufacturing Facility - Omaha, NE: Investigation of collapse
- Quality Time Lanes - Independence, KS: Investigation of roof collapse

Roofing and Waterproofing

- Academy of Holy Angels - Richfield, MN: Roof replacement design and construction observations
- Hennepin County Government Center - Minneapolis, MN: Investigation and repair of waterproofing and expansion joint issues
- Mortenson Construction - Minneapolis, MN: Roof replacement design and construction observations

Structural Evaluation

- Becker-Hanson Building - Pierre, SD: Inspection of corrosion damage and repair design
- Central MN Ethanol Co-op - Little Falls, MN: Evaluation of fire damage to concrete silo
- Cold Spring Brewery - Cold Spring, MN: Investigation of wall cracking and deflection distress at concrete digester
- Congregational United Church of Christ - Ladysmith, WI: Assessment of tornado damage
- St. Mary's University - Winona, MN: Evaluation of Sheffield tile floor structures
- The Union Depot - St. Paul, MN: Condition assessment of train deck structure and construction observations during repair
- U.S. Naval Facility - Quantico, VA: Investigation and repair of reinforced concrete digester

EDUCATION

- University of Minnesota
 - Bachelor of Civil Engineering, 1997
 - Master of Science, Structural Engineering, 1999

PRACTICE AREAS

- Bridge Engineering
- Facade Assessment
- Failure Investigation
- Fire Damage Investigation
- Leakage Investigation
- Roofing and Waterproofing
- Structural Evaluation
- Wind Damage Investigation

REGISTRATIONS

- Professional Engineer in IA, KS, MN, ND, and NE
- PTI Certification for Level 1 Bonded PT - Field Installation
- NHI Course 130078 - Fracture Critical Inspection
- Certified EIFS Industry Professional

PROFESSIONAL AFFILIATIONS

- Post-Tensioning Institute (PTI)

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Objectives

I am a leader. Over the course of a 30+ year working career I have led men and women in combat, as a corporate executive and as an entrepreneur. I am seeking a new opportunity that will allow me to expand my leadership portfolio and experience and to allow my new firm the opportunity to exceed their expectations in hiring a seasoned, thoughtful and passionate construction & technology leader.

Education

University of St. Thomas in Minneapolis

2015 Numerous Executive Education courses including Project Management, Social Media, & Leadership

University of Wisconsin-Madison

June 2001 Masters of Business Administration

University of Missouri-Columbia

May 2003 Bachelor of Science in Business Administration, Minor in Political Science

Experience

Right Stuff Drones, Inc. | 5201 Eden Ave., Suite 300 Edina, MN. 55436

May 2015 – present (13 months)

As CEO & Chief Pilot I am responsible for providing strategic leadership for the company to develop/establish long-range goals, strategies, plans and policies. RSD is an entrepreneurial drone start-up based in the Twin Cities area. The firm has been selected as a 2016 MN Cup Semi-finalist, MN Cup is the largest statewide new venture competition. Key tasks:]

- Completed more than 50 hours on Flight Training leading to an FAA-issued Pilot Certificate
- Developed brand strategies including complete identity creation, website implementation and social media strategies.
- Provided education and training to numerous construction trade organizations on the use of drones.

Target Corporation | 1000 Nicollet Mall, Minneapolis, MN. 55402

June 2006 – May 2015 (9 years)

As a National Construction Executive (Director-level) I managed a large team of Project Managers and Owner's Representatives at Target headquarters & across the United States. I specifically led Regions 100, 200 & 300 and implemented as much as \$1 billion of work in place per year. I was responsible for leading PMs, OSRs and the General Contractor corps to implement construction strategies that included New Stores, Remodel Stores, City Targets, Target Express and numerous other facility management and disaster response.

Mike Korman



- Consistently rated a top leader within the Pyramid and within Target, I served as a mentor to many junior AND senior leaders throughout the company.
- A fixer, I was consistently selected to lead the toughest projects that the company had to offer.
- Served as the quasi Chief Technology Officer (CTO) for the Property Development pyramid and implemented numerous technology initiatives including roll outs across the enterprise.

United States Navy | 1000 Navy Pentagon, Washington D.C. 20350

March 1987 – June 2006 (20 years)

I retired as a Master Chief Petty Officer from the US Navy Seabees. Trained as a Heavy Equipment Operator I served in every enlisted rank from Seaman Recruit (E-1) to Master Chief (E-9). A veteran of four combat deployments, I served in Operation Desert Storm (1991), Bosnia (2001-2002), Kosovo (2003-2004) and Iraq (2005-2006). In Iraq I was specifically selected by name to serve on the leadership staff of General David Petraeus.

As a Command Master Chief I was tasked with representing Sailors in all matters to the Commanding Officer and responsible for active communication throughout the Chain of Command. I advise the commander or commanding officer and provided input in the formulation, implementation, and execution of policies concerning morale, job satisfaction, discipline, family support and training of enlisted Sailors, as well as provide input and advice in matters affecting mission and operations.

- Managed progressively increasing responsibility for facility operations under US Military and NATO operations across Europe and the Middle East.
- Consistently rated a top performer in all ranks with verifiable top scores and ratings every year.
- Recipient of 13 personal awards including a Bronze Star Medal in Iraq.
- In the US Navy, by law...no more than 1.25% of Sailors may hold the rank of Master Chief.

Skills

- Lead, mentor, advise and create cohesive teams that execute assigned tasks, projects and strategies.
- I am a committed lifelong learner. I seek to advance my knowledge through classes both in-person and online.

References

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AGENDA

- Navigating the Waters of Performance and Payment Bonds
- Surprised by Employment - Avoiding and Addressing Misclassification Issues in Minnesota's Construction Industry
- Risk or Reward?
- Multi-State Construction
- Coverage / Legislative Update
- Drones in Construction: Technology, Laws, and Insurance

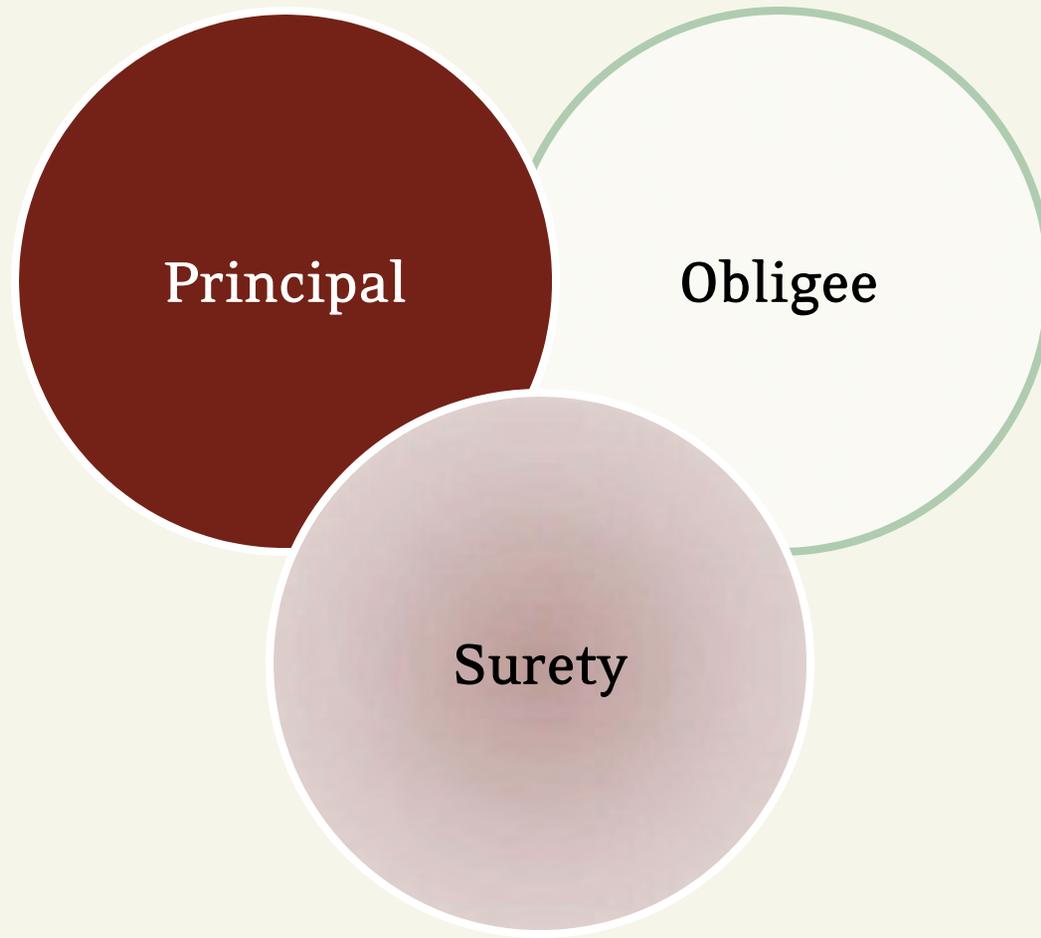
NAVIGATING THE WATERS OF PERFORMANCE AND PAYMENT BONDS

STEPHEN M. WARNER AND
PAUL S. ALMEN

ARTHUR CHAPMAN
KETTERING SMETAK & PIKALA, P.A.

ATTORNEYS AT LAW

WHAT IS A SURETY BOND?



FUNDAMENTALS OF SURETY BONDS

Surety Bonds

- Regulated by state insurance departments
- Prequalification intended to prevent loss
- Three-party agreement
- Coverage is project-specific
- Bond forms are standard or may be negotiated by owner or surety and contractor

Traditional Insurance

- Regulated by state insurance departments
- Spreads fortuitous losses among a large group of similar risks
- Two-party agreement
- Coverage usually term-specific and renewable
- Policy forms vary by insurance company

FUNDAMENTALS OF SURETY BONDS

(continued)

Surety Bonds

- Coverage: 100% of the contract price for performance and 100% for payment, up to penal sum of bond
- Claims - Surety has right to contract balance and indemnity from contractor (contractor remains primarily liable)
- Bonds are required by law in public projects and voluntarily by private owners

Traditional Insurance

- Coverage up to policy limit, less the deductible
- No right to insured's assets, however, companies can subrogate against a third party or another insurer
- Buying insurance is a voluntary way of managing risk of loss for the insured

BENEFITS OF SURETY BONDS

Surety Bonds



Provide capable and qualified contractors

Assure project completion

Offer financial security

Technical, managerial, or financial assistance

BENEFITS OF SURETY BONDS

Surety Bonds



Reduce risk of liens filed by subcontractors, laborers and suppliers

Protect taxpayer dollars

Smoother transition from construction to permanent financing

Lower costs

SURETY BONDS - MORE DEFINITION

Contact Bond

- Three-party agreement
- Guarantees
 - Work completed in accordance with contract documents (plans, specifications)
 - All construction costs will be paid
 - Labor, benefits, payroll taxes
 - Materials
 - Subcontractors

SURETY COVERAGE?

- Regardless of the reason, if the prime contractor fails to fulfill its contractual obligations, the surety must assume the obligations of the contractor and see that the contract is completed, paying all costs up to the face amount of the bond. (in the book)
- Not just provide money to get the project completed but actually responsible for finishing the contract.

ADDITIONAL INFORMATION

- Bond can not be invoked until the contractor is in formal breach of the contract.
- Contract bonds are always written documents.
- Obligations of the bond = provisions of the contract.
- Required on public projects by law.
- Not required by law on private projects - owner's call.
- The dollar amount in which the bond is written for is called the “penalty amount.”

SURETY BONDS MANDATED ON PUBLIC WORKS

- Federal
 - Heard Act (1894)
 - Miller Act (1935)
- State & Local
 - “Little Miller Acts”

THE MILLER ACT

- Enacted in 1935.
- All federal projects greater than \$25,000 - performance and payment bond required.
- 100 percent of the contract amount.
- Protects first and second tier subcontractors only.
- Cannot sue on the payment bond until 90 days after the last day labor was performed on job.

COMMON FORMS

- Indemnity
- Miller Act and Little Miller Acts
- Custom
- American Institute of Architects (AIA)
- ConsensusDocs

KNOW YOUR BOND BEFORE YOU SIGN

- Performance bonds and a payment bonds have terms and conditions that are included in the form itself.
- Along with the terms of the construction contract.
- These terms determine the risk undertaken by the surety and contractor.

ANATOMY OF A BOND

Three parts

- The first part is the “binding paragraph.”
- It identifies the three parties to the bond and states that the surety and principal (the contractor) are jointly and severally bound to the obligee (the project owner).
- This paragraph also establishes a financial limit to the obligation owed to the project owner.
- This limit is called the “penal sum.”

ANATOMY OF A BOND - PART 2

The second part of a bond form is usually quite short, and much of the substance of the obligation is included in the construction contract. Thus, the construction contract is included in the bond form by reference.

- The conditions of this obligation are such that whereas the Principal entered into a certain contract, hereto attached, and made a part hereof, with
- The next paragraph includes the condition and coverage of the bond. It usually states that the condition of the obligation under the bond is that the contractor will perform the contract. If the contractor so performs, then the bond is “null and void.”

ANATOMY OF A BOND - PART 3

NOW THEREFORE, the condition of this obligation is such that, if the Principal shall faithfully perform the said Contract in accordance with the Plans and Specifications and Contract Documents, and shall fully indemnify and save harmless the State of _____ from all cost and damage which the State of _____ may suffer by reason of Principal's default or failure so to do and shall fully reimburse and repay the State of _____ all outlay and expense which the State of _____ may incur in making good any such default, then this obligation shall be null and void, otherwise it shall remain in full force and effect.

PERSONAL GUARANTY

Requiring no specific explanation beyond its name, a Personal Guaranty is good only to the extent of the assets of the entity or individual issuing it. It is subject to the inconvenience and uncertainty of having to do one's own due diligence with regard to those assets, and to the ability of the issuer to cause the Principal to perform. With the threat of personal liability being the primary motivating factor, the value of the Personal Guaranty is limited by both the integrity of the issuer and his, her or its continuing financial viability.

ONEROUS BOND PROVISIONS

- Unduly burden one party
- Hamper competition
- Impact pricing
- Flow down to lower tiers
- Eliminate use of smaller contractors

EXAMPLES OF ONEROUS PROVISIONS

- Automatic Increase in Penal Sum
- Consequential Damages
- Pay when paid
- No liens
- Long term Warranties
- Waiver of Notice of Default
- Short take over timeline (3-7 days)
- Limit Surety options to only one

TYPES OF BONDS

- Bid
- Performance
- Payment

BID BOND

- Guarantees the owner that the contractor will honor its bid and will sign all contract documents if awarded the contract.
- Owner is the Obligee.
- Obligee may sue principal (prime contractor) and surety to enforce the bond.
- What happens if principal refuses to honor its bid?

PRIME CONTRACTOR'S THREE PRINCIPLE RESPONSIBILITIES

Prime Contractor's three principle responsibilities:

- Honor its bid and sign all contract documents if awarded the contract.
- To perform the objectives of the contract.
- Pay all cost associated with the work.

CONTRACTOR DOES NOT HONOR THEIR BID

- Principal and surety are liable on the bond for any additional costs the owner incurs in reletting the contract.
- This usually is the difference in dollar amount between the low bid and the second low bid.
- The penalty sum of a bid bond often is ten to twenty percent of the bid amount.

PERFORMANCE BOND

- Guarantees:
 - Contract performed
 - Owner receives its structure
 - Build in accordance with contract
- Covers warranty period (normally one year).
- Premium includes warranty period coverage.
- If the principal defaults what are the options for the surety?

PERFORMANCE BOND: PRE-CONDITIONS TO SURETY'S OBLIGATIONS

- How are the surety's obligations triggered?
- AIA A312:
 - No owner default
 - Considering declaring in default
 - Request for meeting (optional)
 - Declaration of default and termination
 - Agreement to pay balance of contract price
- ConsensusDocs 260
 - No owner default
 - "Contractor is in Default pursuant to the Contract and Owner has declared the Contractor in default..."
 - Agreement to pay balance of contract price.

FIVE CHOICES

If principal defaults, or is terminated for default by the owner the surety has four choices:

- Complete the contract itself through a completion contractor.
- Takeover.
- Select a new contractor to contract directly with the owner.
- Allow the owner to complete the work with the surety paying the costs.
- Deny the claim.

PERFORMANCE BOND SURETY'S OPTIONS: COMPLETION BY CONTRACTOR

- Why is this an option?
- How does it work?
 - owner / contractor contract relationship status quo.
- Does surety need owner's consent?
 - ConsensusDocs and AIA both require owner consent.

PERFORMANCE BOND SURETY'S OPTIONS: COMPLETION BY SURETY (TAKEOVER)

- Why is this an option?
- How does it work?
 - New contract between surety and owner.
 - Surety subs to original or new contractor.
- Does surety need owner's consent?
 - ConsensusDocs requires; AIA does not.

PERFORMANCE BOND SURETY'S OPTIONS: TENDER

- How does it work?
 - Surety arranges for completion of the contract by contractor who enters into a direct contract with the owner.
 - New bonds required? Yes.
- Does surety need owner's consent? Yes

PERFORMANCE BOND SURETY'S OPTIONS: PAYMENT OF DAMAGES

- Can surety just pay and walk away?
- AIA A312:
 - With reasonable promptness, after investigation, determine the amount for which it may be liable to the Owner.
 - Surety's liability is limited to the amount of the Bond.
 - Liability may include broader categories of damages including legal, design professional and delay costs.
 - If Owner refuses payment the Owner shall be entitled to enforce any remedy available to the Owner.
- ConsensusDocs 260:
 - Waive its right to complete the Work.
 - Reimburse the Owner the amount of its reasonable costs, not to exceed the Bond Sum less the Contract Balances.

PERFORMANCE BOND SURETY'S OPTIONS: DENY LIABILITY

- Why is this an option?
- How does it work?
 - Surety notifies owner; owner controls completion; may send surety a bill for excess cost and damages.
 - What happens to original subs?
- Does surety need owner's consent? No
- Pros and cons
 - Some owners prefer to control completion.

PERFORMANCE BOND: SURETY'S CAP ON LIABILITY

Is the Bond Amount a Cap on the Surety's Liability?

- AIA A312 (2010):

- If the Surety elects to act under Section 5.1, 5.3 or 5.4, the Surety's liability is limited to the amount of this Bond.
- If the Surety elects to undertake to perform and complete the Construction Contract itself, through its agents or independent contractors, the cap may not apply.

- ConsensusDocs 260:

- Explicitly states bond sum is "maximum amount" of surety's obligation.
- Electing to undertake to perform requires consent but the cap continues to apply.

PAYMENT BOND

- Protection of third parties to contract.
- Guarantees payment of labor and materials used or supplied in the performance of construction.
- Not required on privately financed work - few state statutes.
- Protects against “liens.”
- What are liens?

WHAT ARE “LIENS”?

- Right created by law to secure payment for work performed and material furnished in the improvement of land.
- A lien is recorded (with county recorders office) against the title or deed for a property (land and/or building).
- A Title to your new car will have a “lien holder,” your bank, if you have a car loan.

DEFINITION OF CLAIMANT

Who is entitled to make a claim?

- AIA 312 (2010)

- An entity or individual with a direct contract with the Contractor or with a subcontractor of the Contractor.
- An entity or individual who had rightfully asserted a mechanic's lien against the real property upon which the Project is located.
- Defines what types of “labor, materials and equipment” fall within the coverage of the bond.

DEFINITION OF CLAIMANT

- ConsensusDocs 261
 - An entity or individual with a direct contract with the Contractor or having a contract with a subcontractor having a direct contract with the Contractor.
 - Does not extend to those have mechanic's lien rights or specifically define the type of "labor, materials and equipment" falling within the coverage of the bond.

CONDITIONS OF SURETY'S OBLIGATIONS

- Contractor fails to make prompt payment of amounts due.
 - Defenses under subcontract or purchase order available.
- Second tier claimants must wait until payment not made within 90 - 120 days after last work under ConsensusDocs.
 - No such requirement under AIA.

OWNER'S RIGHTS AGAINST THE BOND

- None expressly stated under ConsensusDocs form.
- Under AIA, express coverage for defense of mechanics liens, contingent on:
 - Lack of Owner default.
 - Owner promptly notifies contractor and surety of claim.
 - Owner tenders defense of claim to contractor and surety.

CONDITION OF 2ND TIER CLAIMANTS RIGHTS

- AIA 312 (2010) - The 1986 version of the form did provide a ripeness requirement. This requirement was eliminated and there is no ripeness requirement in the 2010 document.
- ConsensusDocs 261 - There is no surety obligation until the claim has aged for 90 days.

PAYMENT BOND: NOTICE REQUIREMENTS

Claimant: Direct Subcontractor

- AIA 312 (2010) - Claimants, who are employed by or have a direct contract with the Contractor, have sent a Claim to the Surety (at the address described in Section 13).
- ConsensusDocs 261 - No notice requirement for first tier subcontractors or suppl.

PAYMENT BOND: NOTICE REQUIREMENTS

Claimant: Lower Tier Subcontractor

- AIA 312 (2010) - written notice, stating with substantial accuracy the amount claimed and the name of the party to whom the materials were, or equipment was, furnished or supplied, within 90 days and sent a Claim to the Surety, if notice of non-payment is given by the Owner to the Contractor, that is sufficient to satisfy a Claimant's obligation to furnish a written notice of non-payment.
- ConsensusDocs 261 - written notice to the Contractor, the Owner and the Surety within 90 days after the Claimant last provided or performed, stating with substantial accuracy the amount claimed and the name of the Party to whom the materials were furnished, or for whom the work or labor was provided or performed.
 - Minnesota Statutes allow for 120 days from last day of work.

TIME FOR SURETY TO RESPOND

- Not specified under ConsensusDocs form.
- Under AIA, surety must respond to claimant's claim within 60 days.
 - But failure does not waive contractor defenses except as to undisputed amounts.
- Response must state disputed amounts and basis for challenging disputed amounts.

PAYMENT BOND: LIMITATION PERIOD

- What is the limitations period? - One year unless prohibited by law where the action is filed.
- What triggers the limitation period?
 - AIA 312 (2010) - whichever of the following occurs first:
 - The Claimant sends notice to surety; or
 - The last labor, materials or equipment were provided by anyone.
 - ConsensusDocs 261 - the claimant last provided labor, materials or equipment on the Project.

THE SURETY

- Subject to public regulation - same as insurance industry.
- Approved by the U.S. Treasury Department for government projects.
- *A. M. Best Insurance Reports* - financial ratings for insurance and surety companies.
- Owners can require a minimum Best Rating for the surety.

THE SURETY (*CONTINUED*)

- Owners may name the surety company for the contractor to use - NOT RECOMMENDED PRACTICE, but is LEGAL for private work.
- Contractor typically have one surety (bonding company) that has pre-approved contractor.
- Surety pre-approval takes time and involves a review of audited financial statements and other records.
- Co-sureties - large project - one surety does not have the financial capacity for large risks.

INDEMNITY OF SURETY

- Surety indemnifies the owner against default by the contractor.
- Contractor indemnifies the surety against claims and damages due to contractor's failure to perform.
- Surety is not **legally** obligated to provide payment and performance bond if they provided bid bond - **but always do.**

QUESTIONS & ANSWERS

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SURPRISED BY EMPLOYMENT:
AVOIDING AND ADDRESSING
MISCLASSIFICATION ISSUES IN
MINNESOTA'S CONSTRUCTION
INDUSTRY

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ARTHUR CHAPMAN

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I. What Do We Mean By “Misclassification”?

MISCLASSIFICATION

- Definition: Classifying a worker as an independent contractor when, in reality, the worker is a person's/entity's employee
- Multiple tests can apply
- Fact intensive
- Heavily litigated
- Serious consequences

II. Consequences of Misclassification

CONSEQUENCES . . . FOR EMPLOYEES

- No Right to Minimum Wage
- No Right to Overtime Compensation
- No Right to Family Medical Leave
- No Right to Unemployment Insurance

CONSEQUENCES . . . FOR EMPLOYERS

- Wage-and-Hour Lawsuits
- Wage-and-Hour Class/Collective Actions (i.e., Uber's \$100 million settlement)
 - Claim: Uber violated employment laws
 - Class Size: Nearly 400,000 Drivers
 - Proposed settlement: \$100 million; rejected
- Action by State or Federal Government (the D.O.L. loves these)

NO EXCEPTION FOR MINNESOTA'S CONSTRUCTION INDUSTRY

- Wage-and-Hour Lawsuits (Minn. Stat. § 181.722 cause of action for construction workers)
- Wage-and-Hour Class/Collective Actions (none in Minnesota, yet)
- Action by State or Federal Government (the D.O.L. loves these too)

MINN. STAT. § 181.722

- Available only to: Construction Workers
- Claim 1: Subd. 1 - Misrepresentation
 - Misrepresenting nature of employment relationship
 - Government - employees, or other employers
- Claim 2: Subd. 2 - Requirement or Request
 - “requir[ing] or request[ing]”
 - employee to enter into agreement, or sign document
 - results in misclassification of employee as independent contractor or otherwise does not accurately reflect the employment relationship with the employer

MINN. STAT. § 181.722

- No real guidance from Courts
 - Enacted in 2005
 - *Schmidt v. DIRECTV, LLC*, No. CV 14-3000 (JRT/JSM), 2016 WL 519654 (D. Minn. Jan. 22, 2016)
 - Did not apply in *Schmidt* because Plaintiffs were satellite TV installers, not construction workers

MINN. STAT. § 181.722

Consequences of violating Minn. Stat. § 181.722

- Civil damages
- Attorney fees
- Mandatory reporting to State and Federal Agencies

“WAR” ON MISCLASSIFICATION

“[M]ost workers are employees under the [Fair Labor Standards Act]’s broad definitions.”

“The language in the guidance tries to stretch the definition of employee and ‘essentially declares war on the use of independent contractors in certain industries’ such as . . . construction[.] . . . The National Association of Home Builders . . . blasted the new guidance as improperly introduced without public vetting”

“WAR” ON MISCLASSIFICATION

- Minneapolis example
 - Claim: Employees of Minneapolis roofing company misclassified as Independent Contractors
 - Investigation: Interviews and payroll review
 - Conclusion: Misclassification
 - Consequences: Employer Pay \$65,526 in back pay
- More recent awards (2015)
 - \$200k misclassified construction workers in OK
 - \$700k misclassified construction workers in UT & AZ

III. Avoiding Misclassification Issues Under Minnesota Construction Law

EMPLOYEE OR CONTRACTOR?

BURDENSOME TEST

- Test: Minn. Stat. § 181.723, subd. 4.

- Test applies a presumption

Worker = Employee

E'R / GC ≠ Employer

- 1) Registered under Minn. Stat. § 326B.701

AND

- 2) Satisfy 9 factors under Minn. Stat. § 181.723, subd. 4

REBUT THE PRESUMPTION

Nine Factors to Rebut the Presumption

1. Separate business
2. Fed. Tax id. num. or business or self-employment income tax returns
3. Operating under contract to perform the specific service
4. Incur the main expenses related to the service
5. Responsible for satisfactory services

REBUT THE PRESUMPTION

Nine Factors to Rebut the Presumption

6. Receive compensation on a commission, per-job, or competitive bid basis
7. Realize a profit or suffer a loss
8. Continuing or recurring business liabilities or obligations
9. Success or failure business depends on the relationship of business receipts to expenditures

ENSURE REGISTRATION

Check Registration on MN DOLI Website

Detail	Name	Classification Type	License No	Status	Orig Date	Effective Date	Exp Date
Detail	AARON CARLSON CORPORATION	CONTRACTOR REGISTRATION	IR656708	ISSUED	9/28/2012	1/1/2016	12/31/2017
Detail	AARON CARLSON WOODWORK	CONTRACTOR REGISTRATION	IR656850	EXPIRED	10/1/2012	10/1/2012	12/31/2015
Detail	ADAM CARL ZUEHLKE	CONTRACTOR REGISTRATION	IR684767	EXPIRED	8/16/2014	8/16/2014	12/31/2015

ENSURE REGISTRATION OR EXEMPTION

Eight Bases for Exemption:

1. Current license, certificate, or registration under Chapter 299M or 326B
2. Current independent contractor exemption certificate
3. Given a bond
4. Employee of a person in compliance with laws related to employment

ENSURE REGISTRATION OR EXEMPTION

Eight Bases for Exemption:

5. Architect or professional engineer
6. School district or technical college governed under Chapter 136F
7. Providing construction services on volunteer basis
8. Exempt from licensing under Minn. Stat. § 326B.805, subd. 6, clause (5)

III. Addressing Misclassification Issues Under Minnesota Construction Law

LAWSUIT UNDER MINN. STAT. § 181.722

- Step 1: Ensure registration under Minn. Stat. § 326B.701 and satisfy 9 independent-contractor factors in § 181.723.
- Step 2: Check the MN DOLI website.
- Step 3: Check 8 registration exemptions.

QUESTIONS & ANSWERS

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RISK OR REWARD?

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ATTORNEYS AT LAW



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October 13, 2016



Overview

Traditional
Trend

Overview

Traditional Construction Defect Lawsuit

- HOA files lawsuit
 - Specific allegations
 - Vague allegations
- HOA hires Consultant
 - Investigation (limited)
 - Opinions
 - Recommendations
- Defendants hire consultants
- Repair Estimates
- Litigation
- Resolution

STATE OF MINNESOTA	DISTRICT COURT
COUNTY OF RAMSEY	SECOND JUDICIAL DISTRICT
Western Row Condominium Association,	Case Type: Other Civil
Plaintiff,	File Number: _____
v.	AMENDED COMPLAINT
Duxbury Associates, LLC; John Wall, individually; Bor-Son Construction, Inc.; Bor-Son Building Corporation; Bor-Son, Inc.; Boarnan Kroos Vogel Group, Inc.; Minnesota Vinyl & Aluminum, Inc.; Kelleher Construction, Inc.; Kremer & Davis, Inc.; Innovative Building Concepts, Inc.; Central Roofing Company; Dziejdzic Caulking, Inc.; Pella Windows & Doors - Twin Cities, Inc.; Olympic Wall Systems, Inc.,	
Defendants.	

Overview

Trend in Construction Defect Lawsuits

- HOA files lawsuit
 - Specific allegations
 - Vague allegations
- HOA hires Consultant
 - Investigation (limited)
 - Opinions
 - Recommendations
- Defendants hire consultants
- Litigation
 - **HOA performs repairs**
- Resolution



Overview

Why Repairs During Litigation? One nerd's opinion....

- Problems are problematic
 - Leaks and safety issues

- Simplify/reduce points of contention
 - Actual scopes, damages and costs

- Unforeseen conditions
 - **There will always be surprises**

- If you can afford it....why not?



Overview

Distinction

Issue	Traditional	Trend
Scope	Unknown <i>Systemic vs. Local?</i>	Known <i>Could Help or Hurt</i>
Cause	That Guy →	← That Guy
Significance	Actual vs. Virtual Problems	Actual Problems <i>and "Glad We Found Its"</i>
Cost	Projected <i>Contractor A vs. Contractor B</i>	Incurred

Overview

Trend – Impact on Typical Issues

- Scope
 - It may be bigger or smaller than you expect
- Cause
 - Testing is often off the table  speculation
- Significance
 - Justification on the fly?
- Cost
 - Real dollars have been spent

Overview

Trend – Impact on Typical Issues

- **Scope**
 - It may be bigger or smaller than you expect
- Cause
 - Testing is often off the table → speculation
- **Significance**
 - Justification on the fly?
- Cost
 - Real dollars have been spent



Overview

Focus on Scope and Significance

Three Outcomes (generally):

1. Lots of Damage  The work was probably warranted
2. THE GREY ZONE  Would this be a problem later?
3. Everything Looks Good Everywhere  The least likely outcome

Overview

Focus on Scope and Significance

Three Outcomes:

1. Lots of Damage



The work was probably warranted

2. THE GREY ZONE



Would this be a problem later?

3. Everything Looks Good Everywhere



The least likely outcome



Case Studies

#1 – Traditional

#2 – Trend - The Grey Zone

#3 – Trend - Different than expected

Case Study #1 – Richfield Condo

Overview

- 4 story building + townhomes
- Multiple claddings
 - Fiber cement panels
 - Metal panels

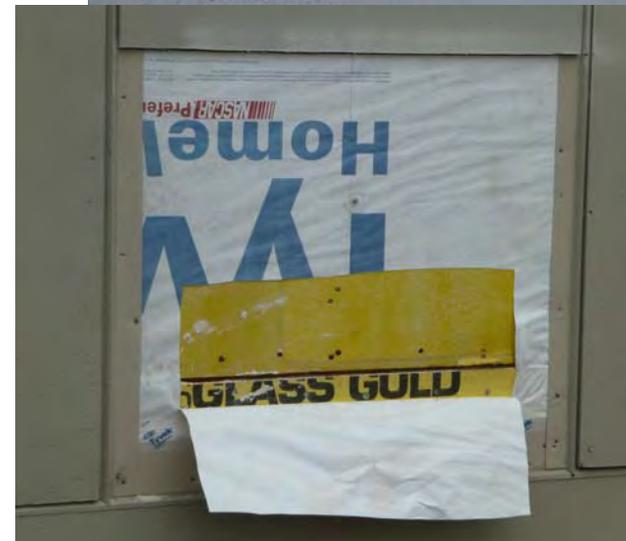


Case Study #1 – Richfield Condo

Dispute

Issues

- Fiber Cement Siding
 - Loose panels and workmanship issues
 - Design criticisms
 - One small area of moisture damage
- Metal Panels
 - Workmanship Criticisms
 - Not installed per instructions
 - No moisture damage
 - “but its probably there”*



Case Study #1 – Richfield Condo *Dispute (Continued)*

HOA

- Remove and replace all metal panels
 - No warranty since not per instructions
 - Probably damage behind it
- Remove and replace all fiber cement siding
 - Probably damage behind it

Others

- Fix the loose siding panels (20%)
- Metal panel deviations are insignificant
- No evidence of systemic damage

Scope Debate

Case Study #1 – Richfield Condo

Results

- Expert mediation
 - Not productive
 - No movement

- Legal proceedings
 - Deposition testimony that loose panels were known > 2 years ago
 - Statute of limitations motions

Case dismissed – statute of limitations

Case Study #2 – St. Paul Condo

Overview

- 4 story brick-clad building
- Multiple balcony stacks
 - 4th floor open
 - 1st-3rd floors inset
- Balcony construction:
 - Concrete topping
 - Waterproofing
 - Plywood
 - Wood framing
 - Fiber cement soffit



Case Study #2 – St. Paul Condo

Dispute

Issues

- Damage @ 4th floor balconies
- Questionable design/details at other balconies that will be problematic
 - But no obvious damage

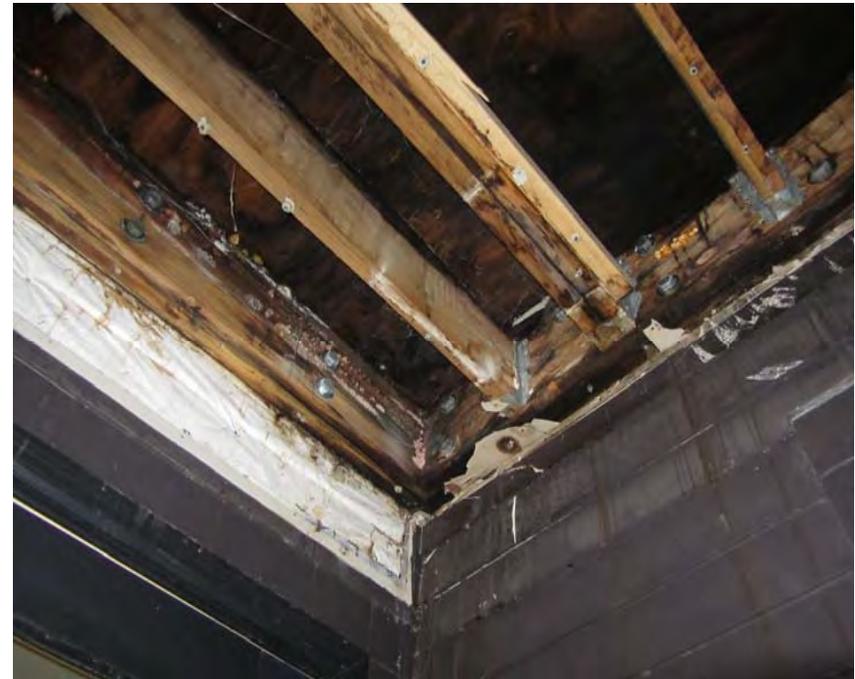
HOA

- Reconstruct all balconies

Others

- Fix the damage

Yet again....Scope Debate



Case Study #2 – St. Paul Condo

Repairs

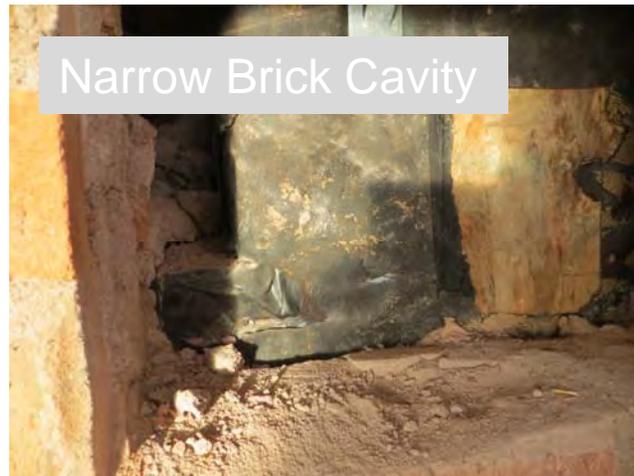
- HOA proceeded with repairs at all balcony areas
- Moisture Damage:
 - 8 of 9 balconies on 4th
 - 2 of 9 balconies on 3rd
 - 0 of 9 balconies on 2nd

But look what else we found....



Case Study #2 – St. Paul Condo

Repairs



Case Study #2 – St. Paul Condo

Results

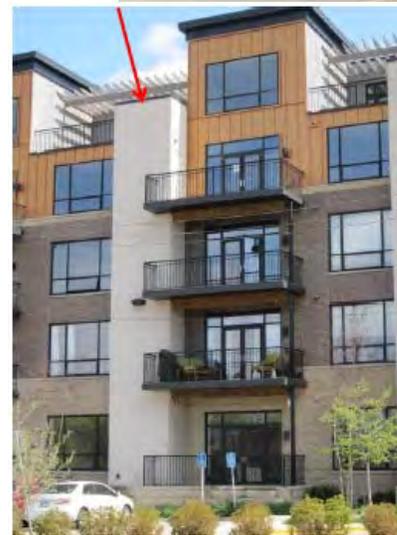
- Claims shifted to damage AND “future” damage
 - Deficiencies/imperfections would leak some day.....
- Outcome:
 - Actual damages generally matched defense position
 - Dispute on non-damaged repair areas flipped to workmanship issues
 - Some fair criticisms.....but the as-built had performed for many years

Settled

Case Study #3 – Minneapolis Condo

Overview

- 4 and 5 story building
- Multiple claddings:
 - Metal Panels
 - Brick
 - CMU
 - Fiber Cement siding
- Mechanical closet stacks (28)
 - Fiber cement siding



Case Study #3 – Minneapolis Condo *Dispute*

Issues

- Loose fiber cement siding panels in “many areas”
 - Nails did not hit studs

HOA

- Remove and replace 100%
 - Safety issue

Others

- Fix the loose panels
 - Less than 5%



Case Study #3 – Minneapolis Condo *Repairs*

- HOA removed and replaced 100 % of fiber cement siding panels
 - Mechanical closets
 - Other areas

*But look what else
we found....*



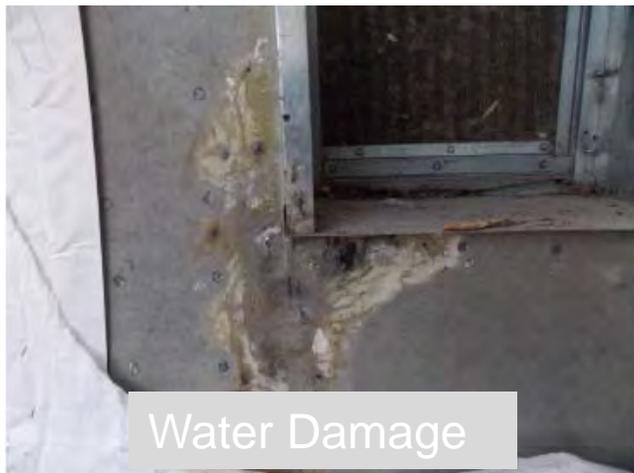
Case Study #3 – Minneapolis Condo *Repairs*



Water Damage



Poor Flashing Details



Water Damage



Condensation Damage

Case Study #3 – Minneapolis Condo

Results

- Outcome:
 - Actual damages greatly exceeded expectations
 - Attachment issue became a moot point
 - New targets emerged to justify completed work
 - Poor flashing details
 - Rim condensation issues
 - Moisture damage at many locations

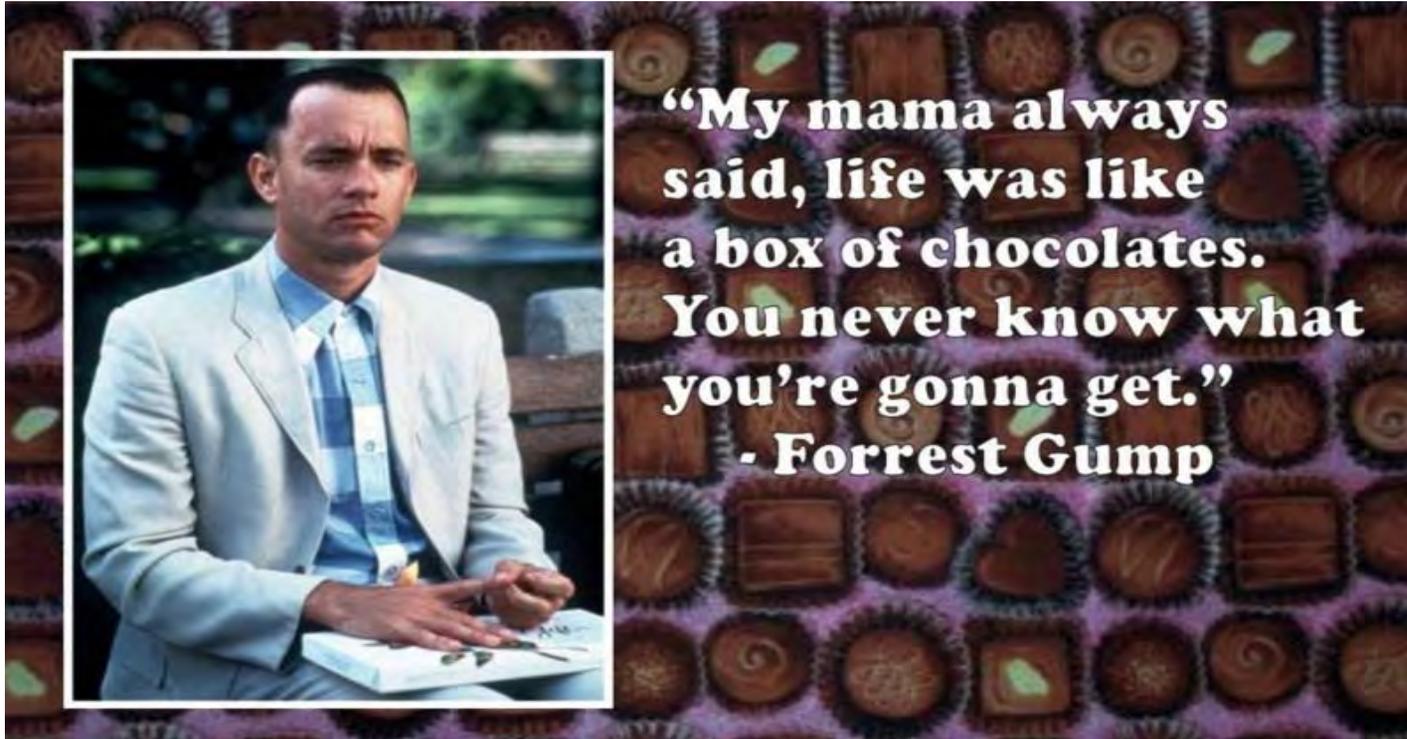
Settled

Case Study #3 – Minneapolis Condo

Epilogue

- Addt'l claims on metal panels:
 - Buckling + crushing “throughout”
 - HOA sued for remove/replace 100%
- Response:
 - Some distortion - aesthetic
 - No investigative work performed
 - No evidence of problem/damage
- Litigated (no repairs)
- Settled this issue too (*likely not favorable to HOA...just my guess*)
- Repaired later by HOA
 - HOA consultant reported significant moisture damage





**“My mama always
said, life was like
a box of chocolates.
You never know what
you’re gonna get.”
- Forrest Gump**

Thanks!

REFRESHMENT BREAK

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MULTI-STATE CONSTRUCTION

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SOL AND REPOSE – MN

- Injury arising from defective or unsafe condition of improvement to real property
- Statute of Limitations: 2 years - “knew or should have known”
- Statute of Repose: 10 years. A claim can still be brought up to 12 years after the date of substantial completion if discovery of the injury occurred in the 9th or 10th year
 - Contribution/indemnity claims must be brought within earlier of 2 years of payment or of being sued and within 14 years after substantial completion

SOL AND REPOSE – ND

- Governs actions in contract or tort for injury to person or property or for deficiency in the design, planning, supervision, or observation of construction or improvement to real property.
- Statute of Limitations/Statute of Repose: 10 years. For injury to property or person occurring in the 10th year, within 2 years of the injury, but not more than 12 years.
- Six year breach of contract SOL
- Three year negligence SOL for property damage

SOL AND REPOSE – WI

- Statute of Limitations: Personal injury and death, 3 years. Property damage, 6 years. Contract, 6 years. Subrogation, same as underlying tort. Contribution and Indemnification for paying a greater share of a common liability, 6 years for contract actions and 1 year for tort actions.
- Statute of Repose: 10 years after substantial completion of improvement, regardless of whether injuries are discovered or the action accrues by that date. Substantial completion ordinarily the date when building is occupied and used for intended purpose.

SOL/REPOSE EXCEPTIONS

- Fraud is an exception in every state to the imposition of the SOL or Repose.
- In WI, actions allowed against an owner or occupier for damages resulting from negligence in the maintenance, operation or inspection of the real property.
- In WI, a person can expressly warrant or guarantee the improvement to real property for a time period longer than the Statute of Repose.

WARRANTY/RIGHT TO CURE – MN

- Minn. Stat. § 327A statutory warranties due to non-compliance with building standards:
 - 1 year warranty that dwelling is free from defects caused by faulty workmanship or defective materials;
 - 2 year warranty plumbing, electrical, and HVAC defects;
 - 10 year warranty free from major construction defects.
- Must provide written notice within 6 months of discovery of loss or damage.
- Right to inspect within 30 days and if inspection, right to make offer of repair. SOL tolled during this period.
- MCIOA 515B implied warranties.

WARRANTY/RIGHT TO CURE – ND

- No statutory warranty.
- Warranty claims commonly asserted as either express or implied warranty claims.
- Implied warranties:
 - Fitness for a particular purpose;
 - Implied duty to provide services in a workmanlike manner.
- Before undertaking repair or instituting action for breach of warranty must provide written notice to contractor within 6 months and give reasonable opportunity (30 days) to inspect or remedy.

WARRANTY/RIGHT TO CURE – WI

- Express and implied warranty, but no statutory.
- Right to cure law enacted in 2005:
 - Written notice of defect must be delivered 90 working days before commencing action.
 - Contractor has either 15 or 25 working days to provide claimant with written 1) offer to repair, 2) offer to settle, 3) combination of both, 4) rejection of claim, or 5) proposal to inspect.
 - If rejected, can commence suit. If offer, 15 days to accept or reject. Additional deadlines for supplemental responses and offers.

ECONOMIC LOSS GENERALLY

- What is Economic Loss?
 - Pecuniary damage for insufficient value, cost to repair or replace, and loss profits, but without any claim of personal injury or damage to other property.
- What is the Economic Loss Doctrine?
 - Common law doctrine
 - Generally holds that when a product defect or failure causes damage to itself and not personal injury or damage to other property a party cannot recover on a tort theory for damages that are purely economic.

ECONOMIC LOSS – MN

- Codified in Minn. Stat. § 604.10
- Economic loss that arises from a sale that is due to damage to property other than the goods sold may be recovered in tort as well as contract unless parties are merchants in goods of the kind.
- Economic loss that arises from sale of goods between merchants that is not due to damage to property other than the goods may not be recovered in tort.
- Exceptions: Fraud or intentional misrepresentation.
- Confused applicability in construction cases since statute is designed to apply to sale of goods.

ECONOMIC LOSS – ND

- The economic loss rule in ND is that economic loss resulting from damage to a defective product may be recovered in a suit for breach of contract or warranty, but not for torts.
- However, the economic loss rule has not been addressed by the ND Supreme Court in a construction context.

ECONOMIC LOSS – WI

- Large body of law on Economic loss in WI.
- Economic loss in WI is damage to the product itself or monetary loss caused by a defective product that does not cause personal injury or damage to other property.
- Economic Loss Doctrine precludes recovery in tort for loss of the product itself that does not cause other property damage or bodily injury.
- Under the integrated system doctrine, component parts integrated into the same system as the defective parts do not qualify as other property.

*650 N. MAIN ASSOCIATION V.
FRAUENSHUH, INC.*

MINNESOTA COURT OF APPEALS HOLDS DEVELOPER
VICARIOUSLY LIABLE FOR DESIGN AND
CONSTRUCTION DEFECTS UNDER MINNESOTA
COMMON INTEREST OWNERSHIP ACT.

*650 N. MAIN ASSOC. V. FRAUENSHUH, INC.
---N.W.2ND ---, 2016 WL 4420781*

ARTHUR CHAPMAN
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ATTORNEYS AT LAW

650 N. MAIN ASSOCIATION V. FRAUENSHUH, INC.

- HOA v. Developer v. General Contractor
 - 327A.02 and MCIOA
 - General Contractor v. Subcontractors
 - Developer - no claim against architect
- Two week trial
 - Major construction defects
 - GC \$101,250 --- no notice - no verdict
 - Design defects
 - Architect (non-party) \$101,250
 - Developer --- no breach of implied warranties, no fault on developer

650 N. MAIN ASSOCIATION V. FRAUENSHUH, INC.

- Post-Trial Motions DC Judge ruled:
 - Developer responsible for design fault \$101,250, plus attorney fees
 - Developer and GC not responsible for \$101,250 because of failure to provide notice
- Court of Appeals:
 - Developer responsible for design fault \$101,250, plus attorney fees - **AFFIRMED**
 - Developer and GC not responsible for \$101,250 because of failure to provide notice - **REVERSED—
DEVELOPER RESPONSIBLE**

650 N. MAIN ASSOCIATION V. FRAUENSHUH, INC.

- Developer vicariously liable for the design-defect damages attributed to architect under MCIOA
 - HOA need not comply with expert affidavit requirements of Minn. Stat. § 544.42 to argue building had design defects. Engineering experts were enough to get in front of jury.
- Developer vicariously liable for the MCIOA
 - Developer breached its warranty by not providing a building that was “constructed in accordance with applicable law, according to sound ... construction standards, and in a workmanlike manner”
- Back to DC - enter GC’s \$101,250, plus additional attorney fees against developer

650 N. MAIN ASSOCIATION V. FRAUENSHUH, INC.

Lessons - future

- Pressure on Developer
 - Burden of Proof on Architect. Affidavit?
- Pressure on GC
 - Developers pushing hard on indemnity
- Pressure on Subs
 - Subs pushing hard on indemnity
- Attorney fees --- real risk under MCIOA

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CONSTRUCTION LITIGATION LANDSCAPE OF YEARS PAST

Then:

- Single family residences
- Limited number of parties
- Little to no use of written contracts
 - Proposal
 - Invoice
- Damages under \$500,000

CONSTRUCTION LITIGATION LANDSCAPE TODAY

Now:

- Multi-unit buildings
- Increased number of parties
 - Multiple subcontractors of same trade
 - Owners, developers, architects, engineers
- Complex written contracts
- Insurance provisions
- Risk transfer
- Damages over \$1,000,000

OVERVIEW

- Applicable Insurance
- History of Risk Transfer
- Minn. Stat. § 337.05 Amendments
 - Changes/trends in industry since 2013
 - Newly proposed amendment
- Additional Insured Endorsements/Insured Contracts

OVERVIEW

- Question from client and insurers
- Significant activity at trial court level
 - Motions for Summary Judgment
 - Declaratory Judgment Actions
- Significant impact on settlement negotiations
- Significant activity at legislative level

INSURANCE

- Common Policies
 - CGL Policy
 - Most Common and Frequently Used
 - Builder's Risk Policy
- Less Common
 - Wrap or "wrap-up" Policy
 - Owner Controlled Insurance Programs (OCIPs)
 - Contractor Controlled Insurance Programs (CCIPs)
 - Typically only used on \$100M plus projects

REFRESHER COURSE

Minn. Stat. § 337.05

BRIEF HISTORY - CONSTRUCTION CONTRACTS PRE-1984

Pre-1984 - Construction agreements that required a subcontractor to indemnify a general contractor for liability resulting from general contractor's own fault were enforceable. *See Seward Housing Corp. v. Conroy Brothers Co.*, 573 N.W.2d 364 (Minn.1998).

- Rule of “Fair Construction”
 - Duty to indemnify could be found by implication, even if not expressly stated.
- Rule of “Strict Construction”
 - Must be expressly stated. Does clause “clearly and unequivocally” demonstrate an intent to shift the risk of loss from general contractor, owner, developer to subcontractor?

BRIEF HISTORY - CONSTRUCTION CONTRACTS 1984-2013

1984 - Anti-Indemnity Statute

- Minn. Stat. § 337.02
 - An indemnification agreement contained in, or executed in connection with, a building and construction contract is unenforceable except to the extent that: (1) the underlying injury or damage is attributable to the negligent or otherwise wrongful act or omission, including breach of a specific contractual duty, of the promisor or the promisor's independent contractors....
- Intent: Prevent contractor from obtaining indemnity for its own fault.

BRIEF HISTORY - CONSTRUCTION CONTRACTS 1984-2013

1984 - Anti-Indemnity Statute Exception

- Minn. Stat. § 337.05
 - § 337.02 does not affect the validity of agreements whereby a promisor agrees to provide specific insurance coverage for the benefit of others.
- Intent: Allow indemnity if coupled with an agreement to provide specific insurance coverage for the indemnity obligation.

NOT SO BRIEF HISTORY *CONTINUED*

Holmes v. Watson-Forsberg, Co., 488 N.W.2d 473 (Minn.1992)

- In our view, the Legislature both anticipated and approved a longstanding practice in the construction industry by which the parties to a subcontract could agree that one party would purchase insurance that would protect “others” involved in the performance of the construction project.

THIS HISTORY IS GETTING BORING

- *Siefert v. Regents of the University of Minnesota*, 505 N.W.2d 690 (Minn.1995)
- *Van Vickle v. S.W. Scheurer and Sons, Inc.*, 556 N.W.2d 2385 (Minn. Ct. App. 1997)
 - Attorney's Fees
 - Tender of defense - condition precedent

ANTI-INDEMNITY STATUTE PRACTICAL APPLICATION

The Court finds that the public policy of the State as expressed in the statutory scheme and the Minnesota Supreme Court's ruling reinstating the district court's decision in *Holmes*, plainly supports the finding that, **unless the Subcontractors failed to procure the required insurance, the indemnity obligation required by the Subcontracts runs from the Subcontractors' insurers, not the Subcontractors themselves.**

Phoenix on the River Homeowner's Association v. Phoenix Lofts, Inc. et. al.

Order on Summary Judgment - July 27, 2015

Hennepin County Court File No. 27-CV-13-17105

ANTI-INDEMNITY STATUTE PRACTICAL APPLICATION

Here, the allegations in Plaintiffs' Complaint implicate all of the Subcontractors. All of the Subcontractors are named as defendants in the Complaint along with the [General Contractor]. The facts alleged in the Complaint also implicate the work of the Subcontractors. Plaintiffs allege defects with roof installation, window installation, ICF installation, foam insulation installation, and stucco application. These allegations relate to work that the Subcontractors contractually agreed to perform and each could be liable to Plaintiffs. Additionally, the [General Contractor] is potentially liable for all of the construction defects Plaintiffs alleged in the Complaint. **Thus, the allegations in Plaintiffs' Complaint arguably create liability for the [General Contractor] arising out of the work of the Subcontractors. As such, the Subcontractors' duty to defend and indemnify is triggered here.**

Laskin v. Stephen Longman Builders, et. al.

Order on Summary Judgment - October 19, 2015

Hennepin County Court File No. 27-CV-15-3621

2013 AMENDMENT/CURRENT STATUTE EFFECTIVE AUGUST 1, 2013

Minn. Stat. § 337.05(b)

A provision that requires a party to provide insurance coverage to one or more other parties, including third parties, for the negligence or intentional acts or omissions of any of those other parties, including third parties, is against public policy and is void and unenforceable.

- Intent: Close the so-called “Insurance Loophole”

2013 AMENDMENT/CURRENT STATUTE

§ 337.05 (c)

Does not affect the validity of a provision that requires a party to provide or obtain worker's compensation insurance, construction performance or payment bonds, or project-specific insurance, including, without limitation, builder's risk policies or owner or contractor-controlled insurance program or policies.

- Direct response to concerns expressed by contractors that these forms of insurance would be precluded.

2013 AMENDMENT/CURRENT STATUTE

§ 337.05(d) - Does not affect the validity of a provision that requires the promisor to provide or obtain insurance coverage for the promisee's vicarious liability, or liability imposed by warranty, arising out of the acts or omissions of the promisor.

- Direct response to concerns that subcontractors would not be responsible to insure general contractor against vicarious liability arising from subcontractor's work.

ANTI-INDEMNITY STATUTE PRACTICAL IMPLICATIONS

Project-Specific Insurance

- Not specifically defined by statute
 - Examples:
 - OCIP
 - CCIP
 - Builder's Risk
- Not defined by Minnesota case law

OTHER STATUTES

Design Professionals

- Architects
- Professional Engineers
- Land Surveyors
- Landscape Architects
- Professional Geoscience

WHAT ABOUT DEFENSE?

- Uncertainty: does the statute only prohibit broad-form *Indemnity*? What about *Defense*?
- The anti-indemnity statute prohibits broad-form “Indemnification Agreements”

Subd. 3. **Indemnification agreement.** "Indemnification agreement" means an agreement by the promisor to indemnify or hold harmless the promisee against liability or claims of liability for damages arising out of bodily injury to persons or out of physical damage to tangible or real property.

- What effect does this have on the Duty to Defend?

PRE-2013 AMENDMENT TO 337.05

Could require broad-form defense and indemnity from downstream parties.

- Including defense and indemnity for upstream party's own negligence.
- Typically, the duty to defend and the duty to indemnify were included within the same provision.
 - *See* AGC Standard Form Subcontract

POST-2013 AMENDMENT TO 337.05

- Can no longer require downstream parties to *indemnify* upstream parties for their own negligence.
- Many Construction Contracts (drafted by upstream parties) now include separate provisions requiring:
 - Broad-form Defense
 - Narrow-Form Indemnity

POST-2013 AMENDMENT TO 337.05

- Does the amendment affect defense?
- It depends on whether the duty to defend is independent of the duty to indemnify.
 - Upstream parties: argue these are two separate obligations.
 - Downstream parties: argue the duty to defend flows from and is limited by duty to indemnify

PREDICTIONS?

- Most construction precedent analyzes defense and indemnity provisions together.
 - Because this was not an issue Pre-Amendment, both could be broad-form.
- Insurance Context:
 - Most case law differentiating between defense and indemnity obligations relates to an Insurer/Insured dispute.
 - Applicable here?

INSURANCE PRINCIPLES

- Duty to defend is broader than duty to indemnify:
 - Extends to every claim that arguably falls within scope of coverage
 - Duty to defend one claim creates duty to defend all claims
 - Duty exists regardless of the merits of the claims
- “Generally, where questions of fact need to be discovered to determine if an insurer has a duty to indemnify, a duty to defend exists.”

ANALOGOUS SJ MOTIONS

- Pre-2013 Amendment lawsuits frequently litigate the question of defense costs vs. indemnity costs in indemnity provisions.
- Counties are split:
 - Hennepin and Ramsey are more likely to separate and enforce defense obligation at Summary Judgment stage.
 - Outer counties are less prone.

PRACTICAL CONSIDERATIONS

Effect on settlement

- Defense costs provided for or excluded
- Owner *Perringer* with Subs
 - “[I]f a non-settling party has cross-claims for both contribution and indemnity, either of which is not covered by the terms of the release, then the settling defendant should continue as a party for the limited purpose of defending against the surviving cross-claim.”

Frey v. Snelgrove, 269 N.W.2d 918, 923 (Minn. 1978)

PRACTICAL CONSIDERATIONS

Is there Coverage?

- Subcontractor vs. its insurer
- *Phoenix Lofts and Sunset Ridge*
 - Henn. Cty. Judge Mel Dickstein recently ruled in both cases (among others) that the duty to indemnify runs from the subcontractor's insurer, not the subcontractor itself, unless the subcontractor failed to procure the required insurance.

PRACTICAL CONSIDERATIONS

Later trial to apportion defense costs?

- Trial within a trial to determine who is at fault for which portion of fees?
- Jury question of whether fees are reasonable?
- Essex on the *Park Owner's Association* - Ramsey County File No.: 62-CV-13-522.

PROPOSED AMENDMENTS

Indemnification agreement

- “Indemnification agreement” means an agreement by the promisor to indemnify, **defend**, or hold harmless the promisee against liability or claims of liability for damages arising out of bodily injury to persons or out of physical damage to tangible or real property.
 - Similar bill proposed for the last two years.

PROPOSED AMENDMENTS

§ 337.05 (c)

- Paragraph (b) does not affect the validity of a provision that requires a party to provide or obtain workers' compensation insurance, construction performance or payment bonds, or ~~**project-specific insurance, including, without limitation,**~~ builder's risk policies, or owner or contractor-controlled insurance programs or policies.

CONTRACTUAL LIABILITY COVERAGE

CGL policy:

- Provides coverage for an insured for “those sums that the insured becomes legally obligated to pay as damages because of ‘bodily injury’ or ‘property damage’ . . . [and the insurer] ha[s] the right and duty to defend the insured against any ‘suit’ seeking those damages.”

INSURED CONTRACT EXCEPTION TO CONTRACTUAL LIABILITY EXCLUSION

2. Exclusions

- This insurance does not apply to: . . .
- b. Contractual Liability
 - “Bodily injury” or “property damage” for which the insured is obligated to pay damages by reason of the assumption of liability in a contract or agreement.
This exclusion does not apply to liability for damages:
...
 - (2) Assumed in a contract or agreement that is an “insured contract” “Solely for the purposes of liability assumed in an “insured contract”, reasonable attorneys’ fees and necessary litigation expenses incurred by or for a party other than an insured are deemed to be damages because of “bodily injury” or “property damage”

INSURED CONTRACT EXCEPTION TO CONTRACTUAL LIABILITY EXCLUSION

“Insured contract” means: . . .

- “f. That part of any other contract or agreement pertaining to your business . . . under which you assume the tort liability of another party to pay for “bodily injury” or “property damage” to a third person or organization. Tort liability means a liability that would be imposed by law in the absence of any contract or agreement.”

EXAMPLE:

HARLEYSVILLE INS. CO. V. PHYSICAL DISTRIBUTION SERVICES, INC.

Facts:

- PDSI leases employees to Transportation companies.
- Miller was a trucking company that leased employees from PDSI.
- An employee (Hughes) of PDSI was injured while working at a Miller facility.
- Hughes sued Miller (not his employer, PDSI) for negligently failing to provide a reasonably safe workplace, among other things.

EXAMPLE:

HARLEYSVILLE INS. CO. V. PHYSICAL DISTRIBUTION SERVICES, INC.

Contract:

- “PDSI hereby indemnifies and saves Miller harmless from any and all claims, actions, or causes of action in any way relating to personnel assigned to Miller” and “PDSI shall obtain insurance against any and all of the above mentioned risks and shall name Miller as an additional insured.”
- Miller tendered defense to PDSI and PDSI notified its insurer, Harleysville, of the claim and asked Harleysville to defend and indemnify Miller.

EXAMPLE:

HARLEYSVILLE INS. CO. V. PHYSICAL DISTRIBUTION SERVICES, INC.

Procedural Posture:

- Harleysville denied coverage, on the basis that PDSI's CGL policy did not cover Hughes's suit against Miller.
- Miller and Hughes settled.
- Miller notified PDSI and Harleysville and requested indemnity.
- Harleysville sought a declaratory judgment on the policy's coverage.

EXAMPLE:

HARLEYSVILLE INS. CO. V. PHYSICAL DISTRIBUTION SERVICES, INC.

The 8th Circuit Court of Appeals, applying Minnesota law:

- Although the policy broadly excludes coverage for bodily injury to “[a]n ‘employee’ of the insured arising out of and in the course of ... [e]mployment by [PDSI],” the policy expressly exempts PDSI’s liability to Miller from this exclusion: “[t]his exclusion does not apply to liability assumed by the insured under an ‘insured contract.’”
- Because the liability at issue in this case arises directly from PDSI’s agreement with Miller, the policy covers Hughes’ injuries despite the fact that the injuries occurred while Hughes was working for PDSI. On the whole, the policy covers PDSI’s liability to Miller for Hughes’ settlement.

QUESTIONS & ANSWERS

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DRONES IN CONSTRUCTION: TECHNOLOGY, LAWS AND INSURANCE

Michael Korman

FAA-Certificated Remote Pilot

Minnesota Commercial License
#19760



ARTHUR CHAPMAN

KETTERING SMETAK & PIKALA, P.A.

ATTORNEYS AT LAW



TARGET







Main Hardware Providers in USA

DJI---China (50%+)
3DR---USA
senseFly---France

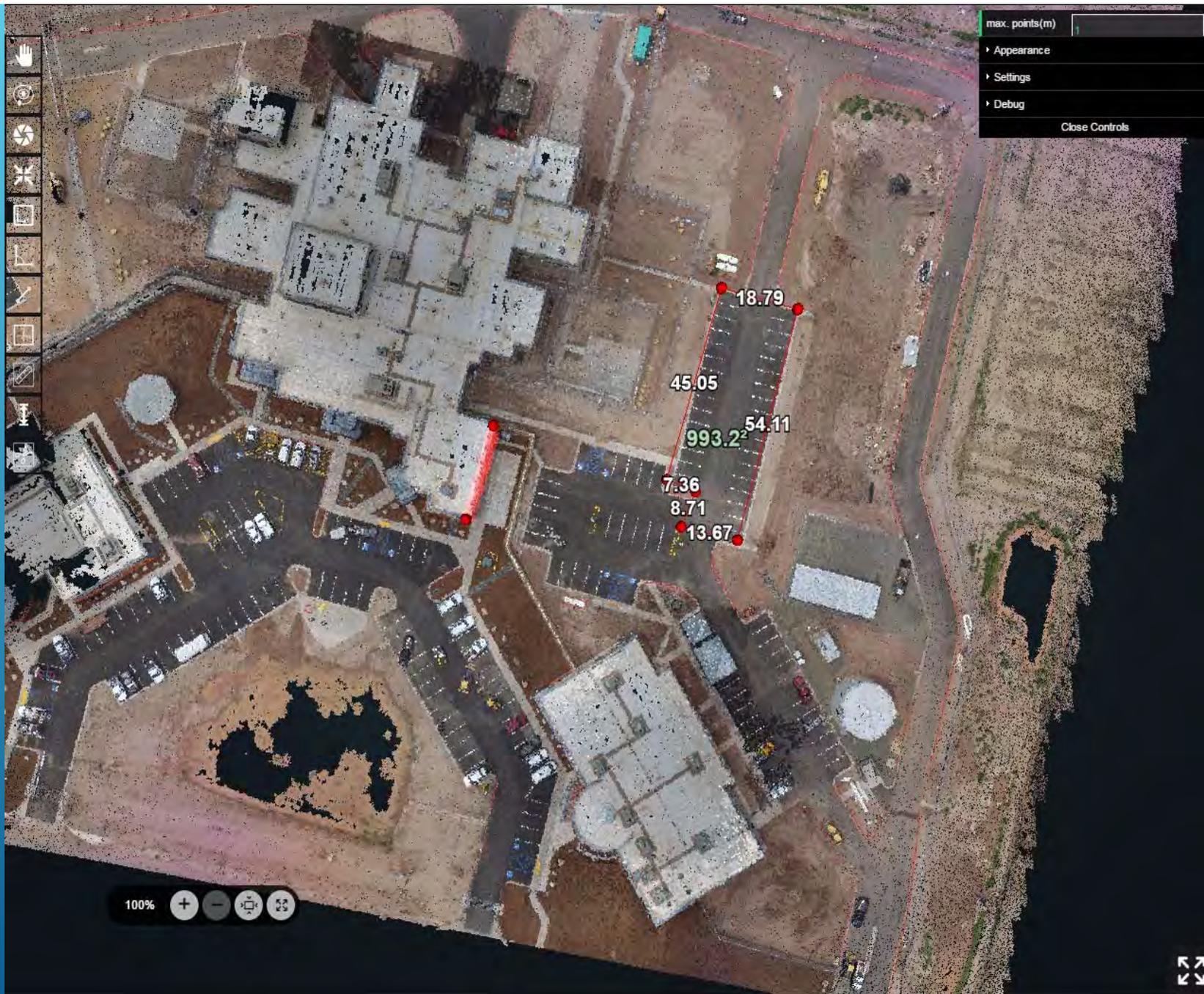


Why Drones and Why Now

Convergence of Miniaturization, Ease of Use and Big Data
Dull, Dirty and Dangerous Jobs

The Secret: Drone aviation is NOT about the aircraft, it is about the sensors and data.







Value	Metric
1000	kB kilobyte
1000 ²	MB megabyte
1000 ³	GB gigabyte
1000 ⁴	TB terabyte
1000 ⁵	PB petabyte
1000 ⁶	EB exabyte
1000 ⁷	ZB zettabyte
1000 ⁸	YB yottabyte

Federal Aviation Regulations (FAR)---FAA.GOV

---Section 333

---Part 107: Small Unmanned Aircraft Regulations

Opening for Business---Drone Aviation is Aviation

I. UNITED STATES OF AMERICA							
DEPARTMENT OF TRANSPORTATION-FEDERAL AVIATION ADMINISTRATION							
II. TEMPORARY AIRMAN CERTIFICATE							III. Certificate No
THIS CERTIFIES THAT							PENDING
IV. MICHAEL JAMES KORMAN							
V. 8113 BEARD AVE S							
EDINA MN 55410							
DATE OF BIRTH	HEIGHT	WEIGHT	HAIR	EYES	SEX	NATIONALITY VI.	
12/4/1968	74 in	240 lbs	GRAY	BLUE	M	USA	
IX. Has been found to be properly qualified and is hereby authorized in accordance with the conditions of issuance or the reverse of this certificate to exercise the privileges of REMOTE PILOT							
Ratings and Limitations							
SMALL UNMANNED AIRCRAFT SYSTEM							
XIII							
THIS IS <input checked="" type="checkbox"/> AN ORIGINAL ISSUANCE <input type="checkbox"/> A REISSUANCE OF THIS DATE OF SUPERSEDED AIRMAN CERTIFICATE							
GRADE OF CERTIFICATE							
BY DIRECTION OF THE ADMINISTRATOR							
EXAMINER'S DESIGNATION NO OR INSPECTOR'S REG NO							
X. DATE OF ISSUANCE							
08/30/2016 09:10:30 PM							
BY SIGNATURE OF EXAMINER OR INSPECTOR							
MANAGER AIRMAN CERTIFICATION BRANCH							
DATE DESIGNATION EXPIRES							
FAA FORM 8060-4 (8-76) USE PREVIOUS EDITION Application ID: 1243609 IACRA Equivalent							
XIV. CONDITIONS OF ISSUANCE							
This is an interim certificate issued subject to the approval of the Federal Aviation Administration pending the issuance of a certificate of greater duration. It becomes void:							
1. Upon the receipt of a certificate of greater duration to replace it.							
2. Upon finding by the FAA that an error has been made in its issuance.							
3. Upon a finding by the FAA that it was issued illegally or as the result of fraud or							
4. Upon the refusal or failure by the holder to accomplish a flight check by a Flight Standards Inspector if so requested; and							
5. In any case, at the expiration of 120 days from date of issuance.							



Pilot Requirements:

- Must be at least 16 years old
- Must pass an initial aeronautical knowledge test
- Must be vetted by TSA

Aircraft Requirements:

- Less than 55 lbs.
- Must be registered with FAA

Operating Rules:

- Class G airspace
- Must keep the aircraft in sight
- Must fly under 400 feet
- Must fly during daylight hours (sunrise-sunset)
- Must fly at or below 100mph
- Must yield right of way to manned aircraft
- Must NOT fly over people
- Must NOT fly from a moving vehicle

***All of these rules are subject to waiver



NOTAMs, TFRs and Airspace

Towered Airports (Notification)

- Class A
- Class B (MSP)
- Class C (KFCM)
- Class D
- Class E



Minnesota DoT Commercial Operations License & Registration

State of Minnesota
Department of Transportation



COMMERCIAL OPERATIONS LICENSE

RIGHT STUFF DRONES, INC.

is licensed for the operations specified below:

AERIAL PHOTOGRAPHY

POWERLINE PATROL

AERIAL SURVEY

UNMANNED AERIAL VEHICLE



Judy Meyers
Authorized Representative

License Number 19760

Expiration Date August 30, 2017

Cassandra Trach
Director, Office of Aeronautics

Mn/DOT TP-08088-02 (6-93)

MINNESOTA DEPARTMENT OF TRANSPORTATION OFFICE OF AERONAUTICS

(651) 234-7201

2016 - 2017 AIRCRAFT REGISTRATION CERTIFICATE

This is to certify that the aircraft designated herein is registered pursuant to Minnesota Statutes 360.511 - 360.67. This certificate will expire at midnight 06/30/2017
This certificate is proof that the aircraft is registered and the tax is paid

N Number	NYKRR4	Make/Model	DJI Inspire 1 Pro
Tax Paid	91.67	Penalty	0.00
Certificate No:	3764	Total	91.67

Michael J Korman
6113 Beard Avenue South
Edina MN 55410



Michael J. Korman
SIGNATURE OF OWNER

If you sell the aircraft, the reverse of the registration certificate must be completed by both the buyer and seller and returned within **seven days** to the Minnesota Department of Transportation, Office of Aeronautics, 222 East Plato Boulevard, Saint Paul, MN 55107-1618

Third Party Operators in Minnesota are required to carry Aviation Liability Insurance.

The Data, its integrity and the Chain of Custody



Who owns the DATA and for how long!!

Risks, Enforcement and Insurance

Commercial Use Drones are NEW!!

- Most platforms are less than 3 years old or considerably less
- Risk profiles are incomplete, difficult to insure accurately
- Recommend that all drone **PICs** carry liability insurance

Federal & State Enforcement Actions

- Operators w/o state license are subject to cease & desist
- Any mishaps w/over \$500 non-drone damage reportable
- Failure to comply with FAA regs, up to \$27,500 fine

Insurance

- Basic Aviation Liability \$1mm = \$875/year
- Errors & Omission coverage, others??

▶ Freedom is Not Free

- ▶ Please consider supporting Veteran-owned businesses

▶ Mike Korman

- ▶ mike.korman@rightstuffdrones.com
- ▶ 847-800-4782
- ▶ @mjkorman



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QUESTION & ANSWER

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ATTORNEYS AT LAW

2016 MINNESOTA CONSTRUCTION LAW SEMINAR

Thank you for attending!

ARTHUR CHAPMAN
KETTERING SMETAK & PIKALA, P.A.

ATTORNEYS AT LAW